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C O N F I D E N T I A L SECTION 01 OF 02 DUBLIN 000966

SIPDIS

E.O. 12958: DECL: 06/29/2014

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SUBJECT: DE PALACIO'S MESSAGE TO U/S LARSON AT US-EU

SUMMIT: LET'S PRESERVE THE STATUS QUO FOR A CIVIL AVIATION
DEAL NEXT YEAR

Classified By: AMBASSADOR JAMES KENNY PER 1.5 (B) AND (D).

1. (U) EUROPEAN COMMISSION VICE PRESIDENT AND COMMISSIONER FOR TRANSPORTATION LOYOLA DE PALACIO MET ON THE MARGINS OF THE JUNE 26 US-EU SUMMIT IN DROMOLAND CASTLE IRELAND WITH UNDER SECRETARY OF STATE FOR ECONOMIC, BUSINESS AND AGRICULTURAL AFFAIRS ALAN LARSON. DE PALACIO REQUESTED THE MEETING TO DISCUSS PROSPECTS FOR A US-EU CIVIL AVIATION AGREEMENT OVER THE NEXT YEAR. SHE WAS ACCOMPANIED BY THE EU'S CHIEF CIVIL AVIATION NEGOTIATOR, MICHAL AYRAL, AND AIDE DANIEL CALLEJA. EUR PDAS RIES AND U.S. NOTETAKERS SAT IN WITH U/S LARSON.

2. (C) DE PALACIO OPENED BY NOTING THAT SHE HAD INVESTED A GREAT DEAL OF EFFORT AND HAD "DONE THE BEST I COULD" TO SECURE A EU-US DEAL, BUT, IN THE END, RECEIVED A VERY DISAPPOINTING ANSWER FROM MEMBER STATES, "ESPECIALLY THE ONE WITH 40 PERCENT OF THE MARKET." SHE NOTED THAT THE MAIN PREREQUISITE FOR THE UK IS SECURING RIGHT OF ESTABLISHMENT (ROE) IN THE U.S. MARKET WHICH SHE ACKNOWLEDGED THE U.S. HAS REPEATEDLY SAID IS NOT POSSIBLE. SHE SAID, HOWEVER, IF THE U.S. DID AGREE TO ROE, "I COULD INITIAL A DEAL TODAY, WITHOUT FURTHER CONSULTATIONS." IF THE U.S. ANSWER TO ROE CONTINUES TO BE "NO", THEN IT WILL BE DIFFICULT TO RESIST THE STRONG PRESSURE FROM MEMBER STATES TO MOVE AHEAD WITH DENUNCIATION OF THE EXISTING U.S. BILATERAL AGREEMENTS WITH MEMBER STATES. SHE SAID FROM ONE POINT OF VIEW DENUNCIATION COULD BE HELPFUL, AS IT WOULD GIVE U.S. AND EUROPEAN PARTIES A ONE YEAR TIMEFRAME TO WORK OUT A NEW ARRANGEMENT. DE PALACIO SAID SHE WAS CONCERNED THAT WITHOUT A DEADLINE A U.S.-EU NEGOTIATION COULD DRAG OUT INDEFINITELY.

3. (C) LARSON REPLIED THAT THE U.S.-EU DEAL THAT WAS REJECTED BY THE EU AT THE JUNE EU TRANSPORT MINISTERS COUNCIL WAS OF GREAT BENEFIT TO BOTH SIDES AND ITS REJECTION A LOST OPPORTUNITY. HE CAUTIONED THAT THOSE IN THE EU INSISTING ON ROE ARE USING IT AS A MEANS TO KEEP A HAMMERLOCK ON THE HEATHROW MARKET; ROE IS A DEFENSIVE, NOT OFFENSIVE PLOY. LARSON SAID IT IS IMPORTANT THAT, IF WE CAN'T GET A DEAL NOW, BOTH SIDES TAKE TIME TO PAUSE, REFLECT, KEEP UP A DIALOGUE, AND THEN MEET AGAIN IN THE FALL. HE STRESSED THAT IT IS IMPORTANT TO PRESERVE THE ARRANGEMENTS IN PLACE THAT ARE BENEFICIAL TO BOTH THE U.S. AND EU AND NOT UPSET THE CURRENTLY BALANCED TRANSATLANTIC RELATIONSHIP.

4. (C) DE PALACIO SAID THAT, ALTHOUGH THE UK HAS 40 PERCENT OF THE MARKET, ROE IS NOT JUST IMPORTANT TO IT BUT TO THE OTHER MEMBER STATES AS WELL. SHE ADDED THAT HER RECENT PUBLIC COMMENTS ON A JULY 15 DEADLINE FOR AN AGREEMENT REFERRED TO THE TIME REMAINING FOR CODIFYING AN AGREEMENT PURSUANT TO CONGRESSIONAL LEGISLATION BUT "THAT IS CLEARLY NOT POSSIBLE NOW." THEREFORE, WE MUST PRESERVE THE CURRENT TEXT AS A STARTING POINT TO RESUME NEGOTIATIONS AT A LATER DATE, WITH THE GOAL OF CONCLUDING A DEAL WITHIN ONE YEAR. HOWEVER, SHE CAVEATED THAT SHE CAN'T PREDICT WHAT THE NEW COMMISSION IS GOING TO DO AND IT WILL BE THEIR CALL AS TO WHETHER TO SET A DEADLINE FOR CONCLUDING AN AGREEMENT. SHE NOTED THAT SHE MUST STILL DISCUSS FURTHER INTERIM STEPS WITH THE COMMISSION IN LIGHT OF THE JUNE TRANSPORT COUNCIL RESULTS. ONE CLEAR RESULT IS THAT U.S. BILATERAL DISCUSSIONS WITH TEN MEMBER STATES ARE SUSPENDED. DE PALACIO ADDED THAT THE ECJ RULING HAS HAD A BROAD EFFECT ON EXISTING U.S. AGREEMENTS WITH MEMBER STATES AND SHE IS BEING SQUEEZED TO DENOUNCE THESE AGREEMENTS. IT WILL BE DIFFICULT TO HOLD THE LINE OVER THE NEXT FIVE MONTHS, AND SHE SUGGESTED A TECHNICAL MEETING IN JULY TO TRY AND GENERATE SOME FORWARD MOVEMENT. EU NEGOTIATOR AYRAL INTERVENED TO SUGGEST THAT SEPTEMBER MIGHT BE MORE CONVENIENT AS IT WOULD GIVE MORE TIME TO FLESH OUT VIEWS/UNDERSTANDINGS ON THE ROE ISSUE.

5. (C) LARSON AGREED THAT SEPTEMBER WOULD BE A USEFUL TIME FOR U.S. AND EU EXPERTS TO CONVENE. IF THE DRAFT AGREEMENT NOW UNDER CONSIDERATION COULD BE PRESERVED, IT WOULD ALLOW NEW MEMBERS OF THE U.S. ADMINISTRATION AND EU COMMISSION TO QUICKLY PICK UP WHERE NEGOTIATIONS LAST CONCLUDED. LARSON STRESSED THAT THE U.S. HAS TRIED TO ADDRESS INTERNAL MARKET ISSUES THAT TAKE INTO ACCOUNT EU INTERESTS, AS WELL AS 49 PERCENT RIGHT OF OWNERSHIP. HE CAUTIONED THAT EU DENUNCIATION WAS A ROAD THE EU DID NOT WANT TO TAKE AS IT POSED LARGE DANGERS: EVEN THOUGH DIRECTED AT MEMBER STATES, IT WOULD BE VIEWED IN THE U.S. AS VERY THREATENING, TANTAMOUNT TO TRADE BREAK/RETALIATION. FURTHERMORE, IT WOULD

GIVE GREATER LEVERAGE TO THOSE FORCES OPPOSED TO A DEAL BY RAISING THE PRICE, CREATING EVEN GREATER HURDLES/ROADBLOCKS FOR THE NEW TEAMS. LARSON SUGGESTED THAT THE FOCUS SHOULD NOW BE ON LEAVING A CIVIL "ROADMAP" FOR THE SUCCESSORS, NOTING THAT THE U.S. HAS ALWAYS BEEN WILLING TO ADDRESS ISSUES RAISED BY THE ECJ. LARSON SAID THAT HE HAD BEEN REFLECTING A GREAT DEAL ON THE UPCOMING POLITICAL TRANSITION PERIOD COINCIDING -- UNUSUALLY -- ON BOTH SIDES OF THE ATLANTIC. HE AGREED THAT IT WAS VERY IMPORTANT DURING THE REMAINING MONTHS UNTIL THE TRANSITION WAS COMPLETED TO KEEP ON AS CONSTRUCTIVE PATH AS POSSIBLE. "WE UNDERSTAND THAT ROE AND YOUR DIFFICULTIES WITH MEMBER STATES WILL STILL BE THERE."

16. (C) DE PALACIO AGREED THAT THE RISK OF FUELING U.S.-EU TRADE TENSIONS WAS THE BIGGEST DOWNSIDE TO EU DENUNCIATION OF EXISTING AGREEMENTS. WHILE NOTING THAT SHE COULDN'T GIVE A FULL ANSWER TODAY, SHE WOULD TRY TO FIND A WAY TO GET MEMBER STATE APPROVAL FOR DEFERRING DENUNCIATION TO HER SUCCESSOR. DE PALACIO STRESSED THAT WHILE DENUNCIATION CAN BE DELAYED, THE NEXT COMMISSION WILL HAVE TO ACT IF THERE IS NO U.S.-EU AGREEMENT. SHE HOPED THAT THE TECHNICAL DISCUSSIONS IN SEPTEMBER WOULD MORE CLEARLY DEFINE THE POINTS OF DIFFICULTY FOR THE NEW TEAM AND CREATE A STARTING POINT FOR CONCLUDING NEGOTIATIONS.

KENNY